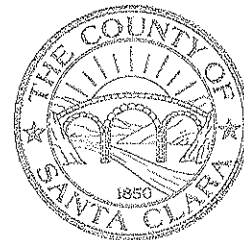


# County of Santa Clara

Office of the County Executive

County Government Center, East Wing  
70 West Hedding Street, 11th Floor  
San Jose, California 95110  
(408) 299-5102  
jeff.smith@ceo.sccgov.org



**Jeffrey V. Smith**  
County Executive

May 21, 2014

Mr. Andrew R. Turnbull  
Managing Director  
Houlihan Lokey  
123 North Wacker Drive, 4th Fl.  
Chicago, Illinois 60606

Dear Mr. Turnbull:

The County of Santa Clara (the "County") is pleased to submit this cover letter (the "Letter") and attached Asset Purchase Agreement (the "APA") describing the terms under which the County would acquire substantially all of the operating assets of O'Connor Hospital ("O'Connor"), Saint Louise Regional Hospital ("Saint Louise"), the DePaul Health Center (together, the "Hospitals"), and Caritas Business Services ("CBS") from Daughters of Charity Health System ("DCHS"). While the Letter is intended to summarize the key terms of the APA, in the event that any discrepancies exist, the APA shall supersede the terms of this Letter. Further, in the event a term has not been defined in this Letter, it shall be construed as having the meaning ascribed to it in the APA.

The County intends to operate the Hospitals and CBS as part of the Santa Clara Valley Health & Hospital System ("SCVHHS"), which serves as the public health and safety-net health care provider for Santa Clara County. With a deep commitment to care for poor and vulnerable populations, grounded both in law and in our operating philosophy, SCVHHS is uniquely positioned within Santa Clara County to continue DCHS' tradition at the Hospitals of providing care to those in need, regardless of ability to pay.

Additionally, the County is confident that it would ensure the most expeditious completion of this transaction. Our acquisition would not require approval from the Office of the Attorney General to complete a transaction with DCHS as would be the case with either an investor owned or not-for-profit acquirer under Cal. Corp. Code section 5915 requiring written consent from the AG or sale of a hospital to "for-profit corporation or mutual benefit corporation or entity" or section 5920 (requiring written consent from the AG for sale of a hospital to "nonprofit corporation or entity". The County's ability to finalize the acquisition without the formal Attorney General review process is expected to shorten the time to close by 90 to 120 days, assuming that other potential partners would receive approval on the first attempt. As the Victor Valley Community Hospital transaction – which closed in late 2012 after nearly two years and the announcement of three different partners – clearly illustrates, the certainty of close is an important consideration in California. Given the monthly cash burn at the Hospitals of approximately \$3 million, which we have estimated using the year-to-date financial statements, our offer preserves at least \$10 to \$15 million of value for DCHS relative to a comparable offer by a private entity that is subject to such Attorney General review. Additionally, we have very positive relationships with labor and are confident that we can work with the Union leadership to quickly transition the DCHS employees to mutually acceptable collective bargaining agreements.

As requested in your letter, below we provide additional information in areas of particular interest:

- **Purchase Price:** The purchase price (the “Purchase Price”) shall be \$150 million payable in cash at closing. Our analysis of the proposed transaction indicates that the total consideration to DCHS would be approximately \$160 million, which includes the Purchase Price and the value of retained working capital by the Hospitals and CBS of approximately \$10 million. Moreover, by eliminating the need for the transaction to be reviewed by the Office of the Attorney General, the County provides DCHS with additional value preservation likely in excess of \$10 million based upon the run-rate cash burn at the Hospitals.
- **Sources of Capital:** The County currently maintains Aa2/AAA/AA+ ratings on its General Obligation debt from Moody’s Investor Service, Standard and Poor’s Rating Services, and Fitch Ratings, respectively. The County, in addition, has a total operating budget of approximately \$4.4 billion and provides an annual support of over \$150 million to SCVHHS to ensure viable health system operations. The County expects to finance the transaction ultimately through the issuance of Lease Revenue Bonds, although it will secure bridge financing or provide internal loans in order to complete the transaction in a timely fashion.
- **Collective Bargaining Agreement:** The County will work to transition employees of the Hospitals to its unions, subject to the terms and limitations set forth in the APA. Based upon a preliminary analysis, we believe that the County offers similar compensation and benefit packages to those provided by DCHS at the Hospitals and has favorable relationships with its union partners.
- **Pension Plans:** The County would not assume DCHS’ liabilities for any retirement, pension, or welfare benefit. Due to the complexity of these claims, we believe that any sale process will need to be validated by a sale order from a bankruptcy court that conveys title free and clear of all liens, claims, and interests.
- **Further Due Diligence:** The County has received access to the DCHS electronic data room; conducted extensive diligence to date, including retaining outside expertise as necessary; and is prepared to commit additional resources to complete its review expeditiously. Within 10 business days of being invited to the next round, we would provide a comprehensive diligence list detailing the items we would need to conclude our due diligence of the Hospitals and CBS.
- **Contingencies:** We believe that the contingencies contained in the APA are standard for a transaction of this nature, and include the satisfactory conclusion of due diligence and approval by the County Board of Supervisors, among others. As mentioned earlier, we also note that our proposal is not subject to a financing contingency or Office of Attorney General review, which could expedite the closing of a transaction by 90 to 120 days.
- **Timing:** The County is prepared to conclude its diligence review within 60 to 90 days of being notified that it is the preferred partner for the Hospitals and CBS, subject to receiving access to requested information and personnel, as reasonable. Should DCHS determine that a bankruptcy process is the proper path, the County is particularly well suited to serve as a Stalking Horse bidder given its ability to close the acquisition more quickly than other potential partners.
- **Purchase Due Diligence:** The County encourages DCHS to review its comprehensive annual financial report and operating budget, both of which are contained on the County’s website ([www.sccgov.org](http://www.sccgov.org)). We are prepared to provide additional information or make our personnel available as requested in order to assist in DCHS’ reverse diligence process.

Thank you for the opportunity to submit this proposal. We look forward to reaching an agreement with DCHS in the near future that best promotes our shared interest of caring for the poor and vulnerable.

Sincerely,

COUNTY OF SANTA CLARA

By: 

Jeffrey W. Smith  
County Executive  
County of Santa Clara

Approved as to Form and Legality:

By: 

Theresa Fuentes  
Lead Deputy County Counsel  
County of Santa Clara

Date: 5/21/14